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## **INTRODUCTION**

The Office of Internal Audit performed a limited scope review of Michigan State Disbursement Unit (MiSDU). The objectives of our review were: to determine if spreading processing over more than one day created any reconciliation or audit trail issues; to verify that all rejected checks were located and were either reprocessed or sent back to the payer; and to evaluate the necessity of the logging and reconciliation process.

The MiSDU currently processes checks received from employers for payment of child support withheld from their employees' pay. Lockheed Martin IMS (LM) operates the MiSDU under a contract with the FIA. LM opens the mail and scans checks received into their record keeping system (TMS). On some days, all of the mail cannot be fully processed through TMS and, therefore, processing takes place over more than one day. The checks that do not get fully processed in a day are stored in a safe. Some of the checks that are originally entered into TMS are rejected for various reasons. TMS provides a rejected check report. These rejected checks are currently listed on a manual log and put into a safe. Some checks are put directly into the safe before they are entered into TMS. These checks have not been rejected by TMS. These checks are considered rejected checks and are listed on the manual log. Rejected checks are subsequently reprocessed or returned to the payer.

## **SCOPE**

We performed a limited scope review of the daily check processing and the check reject process for the period from January 1 through March 31, 2001. Our limited scope review was conducted in accordance with Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

We reviewed the daily check processing documentation for days when processing was spread over more than one day to determine if any reconciliation or audit trail issues were created.

We obtained a description of the check reject process. We also obtained the manual log, system rejects logs, return letters, and reprocess/process documentation related to rejected checks. We tested the process to determine if all checks were either reprocessed/processed or were returned to the payer. We also evaluated the controls that existed over rejected checks.

### **EXECUTIVE SUMMARY**

Based on our review we conclude:

Processing over more than one day did not create any additional reconciliation or audit trail issues.

We tested processing days 1/22, 1/29, and 2/23. For those three days, all checks were either reprocessed/processed, or returned to the sender.

The current logging, tracking, and reconciliation processes are necessary to ensure that the audit trail for every rejected check exists and that those checks are not lost or stolen.

### **MISDU/LM RESPONSE**

MISDU/LM agreed with Findings #1, and 2. MISDU/LM disagrees with Finding #3. They state that their current process provides proven adequate security over the financial instruments and the recommendations would impede their high volume operation. Also if the recommendations were imposed they would need to prepare a cost estimate for the

additional work. For Finding #4, MiSDU/LM stated that they would have the operators set TMS so that all checks are recognized as a check. For Finding #5, MiSDU/LM stated they would continue the logging and reconciliation process, but not necessarily on a daily basis, as they have been doing.

## **FINDINGS AND RECOMMENDATIONS:**

### **Check Processing**

#### **Processing Over More than One Day**

1. Check processing is identified to a “processing day”. LM used two different methods for setting the “processing day” when more than one day was required to process all of one day’s checks received. In one case, LM processed some of the checks, stopped processing without changing the “processing day” and then completed processing the next day. In the other case, LM processed some of the checks, completed their end of the day process for those checks, changed the processing day to the next day and then completed processing the next day. Unprocessed checks were stored overnight in the safe. The choice of different methods creates differences in the daily account reconciliation.

WE RECOMMEND that the MiSDU require LM to chose one specific method of setting the processing day in the situation where a particular day’s mail is processed over more than one day.

## Security

2. We observed that the Southeast corner of the scan room could not be seen on the security camera. Omitting an area of the scan room from security camera coverage increases the risk that checks may be removed without detection.

WE RECOMMEND that the MiSDU require LM to install an additional camera in the scan room to cover the southeast corner.

## Accuracy and Completeness of the TMS System

3. There is no independent record that can be used to determine the accuracy and completeness of the TMS system. Checks are scanned into TMS. Personnel who manually handle the checks prior to scanning do not create check counts or batch counts. Check counts can help ensure that all items are entered into TMS and that the audit trail is started for every check received. There is, apparently, no systematic way of preventing batches from being deleted from TMS other than by policy. Batch counts would help to identify batches that were inadvertently deleted. Also, check counts and batch counts would provide supporting documentation for items that are put into the safe when processing was not completed for a day. Currently, there will be documentation only if the checks have been scanned.

WE RECOMMEND that the MiSDU require the mailroom staff to enter check counts on the batch headers.

WE ALSO RECOMMEND that the MiSDU require the mailroom to number the batch tickets and maintain a log that lists all the batches that went through the

mailroom each day (this was recommended by the SAS70 Auditors in their report).

IN ADDITION, WE RECOMMEND that the MiSDU require LM to reconcile the TMS activity to the batch and check counts from the mailroom on a regular basis.

### **Rejected Checks**

#### Checks not Recognized as Checks by TMS

4. We tested processing days 1/22, 1/29, and 2/23. For these three days, TMS did not recognize 12 checks as checks. These checks were not listed on the TMS rejected check report. They were listed on the manual log for the particular day. Currently, LM is working on an automated log for rejected checks. The source for the rejected items on the log will be TMS. The automated log is meant to replace the manual log. If a check is not recognized by TMS it will not be included in the automated log. The automated log therefore would not be as complete as the current manual log.

The manual log is the only record that documents checks that come directly from the mailroom without being included in a batch.

WE RECOMMEND that LM retain the current logging and reconciliation process until such time as LM can produce an automated log that, without exception, contains all checks and adequately documents the audit trail.

## **Logging and Reconciliation Process**

### **Current Logging and Reconciliation Processes Still Needed**

5. Currently, in order to reduce the chance of theft or loss of a check or ensure that a check can be located, the manual log, the TMS Rejected Check Report, and the reconciliation of one log to the other are necessary.

Getting a check recorded reduces the possibilities for theft or loss. The benefits of getting a check recorded are lost if a rejected check is not recorded and tracked to its ultimate disposition. The manual log in its current form tracks the checks to their ultimate disposition.

The manual log is the only log that contains all items that are in the safe, including checks that came directly from the mailroom.

In the three days we reviewed, the manual log captured the checks that had not been recognized by TMS as being a check.

The TMS Rejected Check Report will identify if there was a check that should be on the manual log but is not and, therefore, it should identify a check that was lost or stolen before it was put on the manual log. Reconciliation of the TMS Rejected Check Report to the manual log by an independent person should detect a lost or stolen check.

The manual logs contain the payer's name, check number, and a check amount, which is useful information to track down a check. The TMS Rejected Check

Report generally (but not always) contains the check number, but does not contain the other information that is useful in tracking down a specific check.

WE RECOMMEND that the MiSDU require LM to track every rejected check to its ultimate disposition.

WE ALSO RECOMMEND that the MiSDU require the LM accountant to continue to reconcile the contents of the safe to the tracking documentation.